

**SCOTT COUNTY HOSPITAL, INC.**

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**FINANCIAL STATEMENTS**

**and**

**ADDITIONAL INFORMATION**

**with**

**INDEPENDENT AUDITOR'S REPORT**

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**YEARS ENDED JUNE 30, 2008 AND 2007**

**George, Bowerman & Noel, P.A.**  
*Certified Public Accountants*

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## INDEPENDENT AUDITOR'S REPORT

Board of Directors  
Scott County Hospital, Inc.  
Scott City, Kansas

We have audited the financial statements, as listed in the table of contents, of Scott County Hospital, Inc., a component unit of Scott County, Kansas, as of June 30, 2008 and 2007, and for the years then ended. These financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the Kansas Municipal Audit Guide. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Scott County Hospital, Inc. as of June 30, 2008 and 2007 and the results of its operations and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audits were made for the purpose of forming an opinion on the basic financial statements taken as a whole. The additional information, as listed in the table of contents, is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audits of the financial statements and, in our opinion, is fairly stated in all material respects in relation to the financial statements taken as a whole.

*George, Bowerman & Noel, P.A.*

Wichita, Kansas  
November 18, 2008

## **SCOTT COUNTY HOSPITAL, INC.**

### **MANAGEMENT'S DISCUSSION AND ANALYSIS**

Our discussion and analysis of Scott County Hospital, Inc.'s (Hospital's) financial performance provides an overview of the Hospital's financial activities for the fiscal years ended June 30, 2008 and 2007. Please read it in conjunction with the Hospital's financial statements, which begin on page 7.

#### **Financial Highlights**

- Unrestricted cash balances increased by \$1,153,871 and \$565,077 or 201% and 263% in 2008 and 2007, respectively.
- The Hospital's net assets increased by \$683,431 or 16.27% in 2008 and by \$68,330 or 1.65% in 2007.
- Gross patient service revenues increased \$542,631 and \$1,492,988 or 4.15% and 12.91% in 2008 and 2007, respectively.
- Contractual allowances and bad debts reduced gross patient service revenue by \$3,771,983 or 27.73% of gross patient service revenue in 2008 and by \$3,795,654 or 29.06% of gross patient service revenue in 2007.
- The Hospital reported operating income of \$119,919 in 2008 and an operating loss of \$247,827 in 2007.

#### **Using This Annual Report**

The Hospital's financial statements consist of three statements—a Balance Sheet; a Statement of Revenues, Expenses, and Changes in Net Assets; and a Statement of Cash Flows. These financial statements and related notes provide information about the activities of the Hospital, including resources held by the Hospital but restricted for specific purposes by contributors, grantors, or enabling legislation.

#### **Financial Statements**

The Hospital's financial statements are prepared using proprietary fund accounting that focuses on the determination of changes in net assets, financial position and cash flows in a manner similar to private-sector businesses. The financial statements are prepared on an accrual basis of accounting which recognizes revenue when earned and expenses when incurred. The basic financial statements include a *balance sheet*, *statement of revenue, expenses and change in net assets*, and *statement of cash flows*, followed by notes to the financial statements and schedules of certain additional information.

The *balance sheet* presents information on the Hospital's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may indicate whether the financial position of the Hospital is improving or deteriorating.

The *statement of revenues, expenses and changes in net assets* presents both the operating revenues and expenses and nonoperating revenues and expenses along with other changes in net assets for the year. This statement is an indication of the success of the Hospital's operations over the past year.

The *statement of cash flows* presents the change in cash and cash equivalents for the year resulting from operating activities, capital and related financing activities and investing activities. The primary purpose of this statement is to provide information about the Hospital's cash receipts and cash payments during the year.

### Financial Position

The Hospital's net assets are the difference between its assets and liabilities reported in the Balance Sheets on pages 7 and 8. The Hospital's net assets increased in each of the past three years as you can see from the following table.

	June 30,		
	2008	2007	2006
Assets:			
Current assets	\$ 3,812,969	\$ 2,538,730	\$ 2,598,111
Capital assets, net	2,870,143	3,269,696	3,890,694
Other noncurrent assets	<u>612,550</u>	<u>662,919</u>	<u>708,564</u>
Total assets	<u>\$ 7,295,662</u>	<u>\$ 6,471,345</u>	<u>\$ 7,197,369</u>
Liabilities:			
Long-term liabilities	\$ 1,158,112	\$ 1,186,834	\$ 1,380,240
Other liabilities	<u>1,254,356</u>	<u>1,084,748</u>	<u>1,685,696</u>
Total liabilities	<u>\$ 2,412,468</u>	<u>\$ 2,271,582</u>	<u>\$ 3,065,936</u>
Net assets:			
Invested in capital assets, net	\$ 1,647,128	\$ 2,067,303	\$ 2,438,907
Restricted	21,994	30,056	53,297
Unrestricted	<u>3,214,072</u>	<u>2,102,404</u>	<u>1,639,229</u>
Total net assets	<u>\$ 4,883,194</u>	<u>\$ 4,199,763</u>	<u>\$ 4,131,433</u>

## Recent Financial Performance

The schedule below is a summary of the Hospital's revenues, expenses and changes in net assets for the past three years.

	Year ended June 30		
	2008	2007	2006
Operating revenue	\$ 9,908,893	\$ 9,373,251	\$ 8,929,884
Operating expenses:			
Salaries	5,245,453	5,241,231	5,047,272
Employee benefits	1,041,238	1,053,179	975,835
Supplies and other	2,768,968	2,564,319	2,664,099
Depreciation and amortization	733,315	762,349	715,044
Total operating expenses	9,788,974	9,621,078	9,402,250
Operating income (loss)	119,919	(247,827)	(472,366)
Nonoperating revenues (expenses):			
Taxes	550,937	338,597	335,165
Investment income	14,821	16,596	14,815
Interest expense	(73,826)	(91,688)	(113,933)
Grants and contributions	48,900	30,152	41,349
Total nonoperating revenues	540,832	293,657	277,936
Excess (deficit) of revenues over expenses before capital grants and contributions	660,751	45,830	(194,970)
Capital grants and contributions	22,680	22,500	155,220
Increase (decrease) in net assets	\$ 683,431	\$ 68,330	\$ (39,750)
Net assets at end of year	\$ 4,883,194	\$ 4,199,763	\$ 4,131,433

### Operating Income (Loss)

The first component of the overall change in the Hospital's net assets is its operating income (loss)—generally, the difference between net patient service and the expenses incurred to perform those services. In 2008 the Hospital reported an operating income of \$119,919 as compared to operating losses of \$247,827 and \$472,366 in 2007 and 2006, respectively.

The primary components of the changes operating income in 2008 are:

- Changes in cost and charge structure and payor mix trends due to a physician terminating practice in the community.
- Decreases in contractual adjustments and bad debt expense as a percentage of gross patient service revenue.
- Significant increase in net patient service revenue while salaries and employee benefits costs remained steady.
- Modest increases in supplies and other costs in relation to significant increase in net patient services revenue.

The rate of healthcare inflation has a direct effect on the cost of services provided by the Hospital. A component of the Hospital's costs are expenses for medical supplies and prescription drugs. Some of the major factors contributing to the increased medical supply and drug costs include the introduction of new drugs that cannot be obtained in generic form, and changes in therapeutic mix.

### **Nonoperating Revenues and Expenses**

Net nonoperating revenues increased \$247,175 in 2008 primarily due to increases in tax support from the County.

### **The Hospital's Cash Flows**

Changes in the Hospital's cash flows are consistent with changes in operating income and losses and nonoperating revenues and expenses, discussed earlier.

### **Capital Assets**

At June 30, 2008, the Hospital had \$2,870,143 invested in capital assets, net of accumulated depreciation, as detailed in Note 7 to the financial statements. In 2008, the Hospital purchased property and equipment costing \$303,774, including \$92,918 for computer equipment, \$48,656 for the East Campus building, \$28,351 towards a new nurse call system, and \$47,978 towards new imaging equipment.

### **Debt**

At June 30, 2008, the Hospital had notes payable and a capitalized lease obligation outstanding of \$976,814 and \$408,536, respectively, as detailed in Note 8 to the financial statements.

### **Other Economic Factors**

Management expects the current economic conditions to continue over the next year.

## **Issues Facing the Hospital**

There are issues facing the Hospital that could result in material changes in its financial position in the long term. Among these issues are:

- Risks related to Medicare and Medicaid reimbursement. A significant portion of the Hospital's revenues are derived from the Medicare program, which provides certain healthcare benefits to beneficiaries who are over 65 years of age or disabled, and the Medicaid program, funded jointly by the federal government and the states, which provides medical assistance to certain needy individuals and families. The funding of these programs by the federal and state governments face increasing pressure due to the significant increases in the costs of providing healthcare services in recent years.
- Employment and labor issues. The Hospital is a major employer within the community, employing a complex mix of professional, technical, clerical, maintenance, dietary, and other workers. Risks include personal tort actions, work-related injuries and exposure to hazardous materials. A relative shortage of nursing and other medical professional/technical employees within the state, is an issue that is causing salary and benefits costs to increase at significant rates.
- Technology and services. Scientific and technological advances, new procedures, drugs and appliances, preventive medicine, and outpatient healthcare delivery may reduce utilization and revenues for the Hospital in the future. Technological advances continue to accelerate the need to acquire sophisticated and expensive equipment and services for diagnosis and treatment of illnesses and diseases.
- Increasing numbers of uninsured and underinsured patients. Due to the significant increases and high cost of healthcare insurance premiums in recent years, increasing numbers of patients of the Hospital are finding it more and more difficult to obtain or maintain adequate health insurance coverage. This trend could increase the levels of uncompensated care provided by the Hospital.

## **Contacting The Hospital's Financial Management**

This financial report is designed to provide our patients, suppliers, taxpayers, and creditors with a general overview of the Hospital's finances and to show the Hospital's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the Hospital Administration Department, at Scott County Hospital, Inc., 310 E. Third Street, Scott City, Kansas 67871.



# SCOTT COUNTY HOSPITAL, INC.

## BALANCE SHEETS

### ASSETS

	June 30,	
	2008	2007
Current assets:		
Cash (Notes 1 and 3)	\$ 1,729,275	\$ 575,404
Assets limited as to use (Note 3)	21,994	30,056
Accounts receivable, net of allowance for doubtful accounts of \$386,867 in 2008 and \$379,530 in 2007 (Notes 1 and 4)	1,572,828	1,375,310
Employee receivable	17,395	13,250
Estimated third-party payor settlements (Note 2)	—	129,789
Inventories (Note 1)	396,147	350,654
Prepaid expenses and other	75,330	64,267
Total current assets	3,812,969	2,538,730
Other assets:		
Employee receivable	140,344	160,725
Goodwill, net of accumulated amortization of \$277,389 in 2008 and \$247,401 in 2007 (Note 1)	472,206	502,194
Total other assets	612,550	662,919
Property and equipment, at cost (Notes 1 and 7):		
Land	56,273	56,273
Land improvements	272,405	272,405
Buildings	3,256,030	3,207,374
Fixed equipment	1,521,352	1,512,796
Movable equipment	5,256,865	5,010,303
	10,362,925	10,059,151
Less accumulated depreciation	7,492,782	6,789,455
Property and equipment, net of accumulated depreciation	2,870,143	3,269,696
Total assets	\$ 7,295,662	\$ 6,471,345

The accompanying notes are an integral  
part of the financial statements.

## LIABILITIES AND NET ASSETS

	June 30,	
	<u>2008</u>	<u>2007</u>
Current liabilities:		
Accounts payable	\$ 330,605	\$ 262,501
Salaries payable	310,210	291,739
Compensated absences payable (Note 1)	220,939	218,445
Payroll taxes payable	127,909	117,933
Estimated third-party payor settlements (Note 2)	35,948	—
Accrued interest payable	1,507	—
Current portion of long-term debt (Note 8)	<u>227,238</u>	<u>194,130</u>
Total current liabilities	<u>1,254,356</u>	<u>1,084,748</u>
Long-term debt (Note 8)	<u>1,158,112</u>	<u>1,186,834</u>
Net assets (Notes 1 and 3):		
Invested in capital assets, net of related debt	1,647,128	2,067,303
Restricted for capital asset acquisition	—	5,000
Restricted for specific operating activities	21,994	25,056
Unrestricted	<u>3,214,072</u>	<u>2,102,404</u>
Total net assets	<u>4,883,194</u>	<u>4,199,763</u>
Total liabilities and net assets	<u>\$ 7,295,662</u>	<u>\$ 6,471,345</u>

# SCOTT COUNTY HOSPITAL, INC.

## STATEMENTS OF REVENUE, EXPENSES, AND CHANGES IN NET ASSETS

	Year ended June 30,	
	2008	2007
Operating revenues:		
Net patient service revenue (Note 1)	\$ 9,831,391	\$ 9,265,089
Outside services	29,348	39,237
Other	48,154	68,925
Total operating revenue	9,908,893	9,373,251
Operating expenses:		
Salaries	5,245,453	5,241,231
Employee benefits	1,041,238	1,053,179
Supplies and other	2,768,968	2,564,319
Depreciation and amortization (Note 1)	733,315	762,349
Total operating expenses	9,788,974	9,621,078
Operating income (loss)	119,919	(247,827)
Nonoperating revenues (expenses):		
Tax revenues	550,937	338,597
Investment income	14,821	16,596
Interest expense	(73,826)	(91,688)
Noncapital grants and contributions	48,900	30,152
Total nonoperating revenues	540,832	293,657
Excess of revenues over expenses before capital grants and contributions	660,751	45,830
Capital grants and contributions	22,680	22,500
Increase in net assets	683,431	68,330
Net assets at beginning of year	4,199,763	4,131,433
Net assets at end of year	\$ 4,883,194	\$ 4,199,763

The accompanying notes are an integral  
part of the financial statements.

# SCOTT COUNTY HOSPITAL, INC.

## STATEMENTS OF CASH FLOWS

	Year ended June 30,	
	2008	2007
Cash flows from operating activities:		
Receipts from and on behalf of patients	\$ 9,799,610	\$ 9,922,987
Payments to suppliers and contractors	(2,757,420)	(2,613,280)
Payments to employees	(5,224,488)	(5,227,011)
Payments for employee benefits	(1,031,262)	(1,045,268)
Other receipts and payments, net	77,502	108,162
Net cash flows provided by operating activities	863,942	1,145,590
Cash flows from noncapital financing activities:		
Property taxes for operations	550,937	338,597
Grants and contributions	48,900	30,152
Principal payments on line of credit	—	(632,748)
Net cash flows provided (used) by noncapital financing activities	599,837	(263,999)
Cash flows from capital and related financing activities:		
Purchases of property and equipment	(303,774)	(111,363)
Grants and contributions for capital assets	22,680	22,500
Proceeds from issuance of long-term debt	200,000	—
Principal payments on long-term debt	(195,614)	(183,066)
Interest payments on long-term debt	(72,319)	(91,688)
Net cash flows used by capital and related financing activities	(349,027)	(363,617)
Cash flows from investing activities:		
Net change in employee receivable	16,236	15,443
Investment income	14,821	16,596
Net cash flows provided by investing activities	31,057	32,039
Increase in cash and cash equivalents	1,145,809	550,013
Cash and cash equivalents at beginning of year	605,460	55,447
Cash and cash equivalents at end of year	\$ 1,751,269	\$ 605,460
Reconciliation of cash and cash equivalents to balance sheets:		
Cash and cash equivalents in current assets	\$ 1,729,275	\$ 575,404
Cash and cash equivalents in assets limited as to use	21,994	30,056
Total cash and cash equivalents	\$ 1,751,269	\$ 605,460

The accompanying notes are an integral part of the financial statements.

# SCOTT COUNTY HOSPITAL, INC.

## STATEMENTS OF CASH FLOWS - continued

	<u>Year ended June 30,</u>	
	<u>2008</u>	<u>2007</u>
Reconciliation of operating loss to net cash provided by (used by) operating activities:		
Operating income (loss)	\$ 119,919	\$ (247,827)
Adjustments to reconcile operating loss to net cash flows used in operating activities:		
Depreciation and amortization	733,315	762,349
Provision for doubtful accounts	293,507	229,507
Net (increases) decreases in current assets:		
Accounts receivable	(491,025)	56,532
Inventories	(45,493)	(35,658)
Estimated third-party payor settlements	165,737	371,859
Other	(11,063)	(12,632)
Net increases (decreases) in current liabilities:		
Accounts payable	68,104	(671)
Salaries and wages payable	18,471	(321)
Compensated absences payable	2,494	14,541
Payroll taxes payable	<u>9,976</u>	<u>7,911</u>
Net cash provided by operating activities	<u>\$ 863,942</u>	<u>\$ 1,145,590</u>

**SCOTT COUNTY HOSPITAL, INC.**  
**NOTES TO FINANCIAL STATEMENTS**  
**June 30, 2008 and 2007**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

This summary of significant accounting policies is presented to assist in understanding the Hospital's financial statements. The financial statements and notes are representations of the Hospital's management, which is responsible for their integrity and objectivity. These accounting policies conform to generally accepted accounting principles and have been consistently applied in the preparation of the financial statements.

**Organization and business activity**

The Hospital is exempt from Federal income taxes under Section 501(c)(3) and is owned by Scott County, Kansas. The Hospital provides acute care, swing-bed, home health, rural health clinic, and outpatient services. The Board of County Commissioners appoints the members of the Board of Directors. For this reason, the Hospital is considered to be a component unit of Scott County, Kansas.

**Enterprise fund accounting**

The Hospital uses enterprise fund accounting. Revenues and expenses are recognized on the accrual basis using the economic resources measurement focus. Based on Governmental Accounting Standards Board (GASB) Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, as amended, the Hospital has elected to apply the provisions of all relevant pronouncements of the Financial Accounting Standards Board (FASB), including those issued after November 30, 1989, that do not conflict with or contradict GASB pronouncements.

**Use of estimates**

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**Operating revenues and expenses**

The Hospital's statement of revenues, expenses, and changes in net assets distinguishes between operating and non-operating revenues and expenses. Operating revenues result from exchange transactions associated with providing health care services – the Hospital's principal activity. Non-exchange revenues, including taxes, grants, and contributions received for purposes other than capital asset acquisitions, are reported as non-operating revenues. Operating expenses are all expenses incurred to provide health care services, other than financing costs.

## **1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES** **(continued)**

### **Cash and cash equivalents**

For purposes of the statement of cash flows, the Hospital considers all highly liquid debt instruments with an original maturity of three months or less to be cash and cash equivalents.

### **Allowance for doubtful accounts**

Accounts receivable is presented net of an allowance for doubtful accounts. The allowance is estimated based on multiple factors including historical experience with bad debts, the aging of receivables, payor mix trends, and local economic conditions. Account balances are written off when determined by management to be uncollectible. If future actual default rates on accounts receivable differ from those currently anticipated, the Hospital may have to adjust its allowance for doubtful accounts, which would affect earnings in the period the adjustments are made.

### **Inventories**

Inventories are stated at cost as determined by the first-in, first-out method.

### **Capital assets**

The Hospital's capital assets are reported at historical cost. Contributed capital assets are reported at their estimated fair value at the time of their donation. All capital assets other than land are depreciated or amortized (in the case of capital leases) using the straight-line method of depreciation using the following asset lives:

	<u>Estimated useful lives</u>
Land improvements.....	10 - 28 years
Buildings .....	15 - 50 years
Fixed equipment .....	10 - 30 years
Movable equipment.....	5 - 21 years

The costs of maintenance and repairs are charged to operating expenses as incurred. The costs of significant additions, renewals and betterments to depreciable properties are capitalized and depreciated over the remaining or extended estimated useful lives of the item or the properties. When depreciable property is retired or otherwise disposed of, the related costs and accumulated depreciation are removed from the accounts and any gain or loss is reflected as non-operating revenue (expense).

### **Goodwill**

Upon acquisition of the Scott City Clinic, P.A., goodwill, which represents the excess of the cost of the clinic stock purchased over the fair value of the net assets of the Clinic, was transferred to the Hospital. The goodwill is being amortized on the straight-line basis over 25 years. Amortization expense charged to operations for each of the years ended June 30, 2008 and 2007 was \$29,988. Amortization expense is expected to be \$29,988 for each of the next five years.

## **1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES** **(continued)**

### **Net patient service revenue**

The Hospital has agreements with third-party payors that provide for payments to the Hospital at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, per diem payments, and discounted charges. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

### **Compensated absences**

Employees of the Hospital are entitled to paid time off depending on length of service and whether they are full or part time. Upon resignation, termination or retirement from service with the Hospital, employees are entitled to payment for all accrued paid time off, up to the allowable maximum. The Hospital accrues the paid time off benefits as earned.

### **Grants and contributions**

From time to time, the Hospital receives grants and contributions from government agencies, private organizations, and individuals. Revenues from grants and contributions are recognized when all eligibility requirements, including time requirements are met. Grants and contributions may be restricted for either specific operating purposes or for capital purposes. Amounts that are unrestricted or that are restricted to a specific operating purpose are reported as non-operating revenue. Amounts restricted to capital acquisitions are reported after non-operating revenues and expenses. When the Hospital has both restricted and unrestricted resources available to finance a particular program, it is the Hospital's policy to use restricted resources before unrestricted resources.

### **Net assets**

Net assets of the Hospital are classified in four components. *Net assets invested in capital assets net of related debt* consist of capital assets net of accumulated depreciation and reduced by the current balances of any outstanding borrowings used to finance the purchase or construction of those assets. *Restricted for specific operating activities* are non-capital net assets that must be used for a particular purpose, as specified by creditors, grantors, or contributors external to the Hospital. *Restricted for capital asset acquisition* are net assets that must be used for the acquisition of capital assets. *Unrestricted net assets* are remaining net assets that do not meet the definition of *invested in capital assets net of related debt* or *restricted*.

### **Risk management**

The Hospital is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; injuries to employees; natural disasters; and employee health benefits. Commercial insurance coverage is purchased for claims arising from such matters. Settled claims have not exceeded this commercial insurance coverage in any of the three preceding years.



## **1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES** **(continued)**

The Hospital pays fixed premiums for annual medical malpractice coverage under an occurrence-basis policy. The Hospital accrues the expenses of its share of malpractice claim costs, if any, of reported and unreported incidents of potential improper professional service occurring during the year by estimating the probable ultimate cost of any incident. Based on the Hospital's own claims experience, no accrual, for medical malpractice costs has been made in the accompanying financial statements.

### **Reclassifications**

Certain reclassifications have been made to the 2007 financial statements to conform to the 2008 presentation. The reclassifications had no effect on the change in net assets.

## **2. ESTIMATED THIRD-PARTY PAYOR SETTLEMENTS**

The Hospital has agreements with third-party payers that provide for payments to the Hospital at amounts different from its established rates. These payment arrangements include:

- **Medicare** – Inpatient and outpatient services are paid based on cost reimbursement methodologies. The Hospital is reimbursed for cost reimbursable items at tentative rates with final settlement determined after submission of annual cost reports by the Hospital and reviews thereof by the Medicare fiscal intermediary. The Hospital's classification of patients under the Medicare program and appropriateness of their admission are subject to an independent review by a peer review organization under contract with the Hospital. The Hospital's Medicare cost reports have been reviewed by the Medicare fiscal intermediary through June 30, 2006.
- **Medicaid** – For the year ended June 30, 2007 and for the period from July 1, to October 4, 2007, inpatient and outpatient services rendered to program beneficiaries are paid at prospectively determined rates. The rates vary according to a patient classification system that is based on clinical, diagnostic and other factors.

Effective with services rendered on or after October 5, 2007, the Hospital is reimbursed under a cost reimbursement methodology for inpatient acute and outpatient services. The Hospital is reimbursed for cost reimbursable items at tentative rates with final settlement determined after submission of annual cost reports by the Hospital and reviews thereof by the Medicaid fiscal intermediary.

Inpatient long-term care services for the years ended June 30, 2007 and 2008 are paid at prospectively determined per diem rates that are based on the patient's acuity.

Approximately 46% and 53% of net patient service revenue is from participation in the Medicare program for the years ended June 30, 2008 and 2007, respectively. Laws and regulations governing the Medicare program are complex and subject to interpretation and change. As a result, it is reasonably possible that recorded estimates will change materially in the near term.

## 2. ESTIMATED THIRD-PARTY PAYOR SETTLEMENTS (continued)

The Hospital has also entered into payment agreements with certain commercial insurance carriers and other third-party payer programs. The basis for payment to the Hospital under these agreements includes prospectively determined rates per discharge, discounts from established charges and cost reimbursement.

## 3. CASH AND ASSETS WHOSE USE IS LIMITED

Cash and assets whose use is limited consisted of the following:

	<u>June 30,</u>	
	<u>2008</u>	<u>2007</u>
Unrestricted:		
Cash on hand	\$ 490	\$ 490
Demand deposit accounts	1,648,347	531,374
Money market accounts	72,196	35,363
Savings accounts	<u>8,242</u>	<u>8,177</u>
	<u>1,729,275</u>	<u>575,404</u>
Assets whose use is limited:		
Cash on hand	1,000	1,000
Money market accounts	<u>20,994</u>	<u>29,056</u>
	<u>21,994</u>	<u>30,056</u>
	<u>\$ 1,751,269</u>	<u>\$ 605,460</u>

Assets whose use is limited are restricted for the following purposes:

	<u>June 30,</u>	
	<u>2008</u>	<u>2007</u>
Hospital services	\$ —	\$ 2,223
Hospital equipment	—	5,000
Emergency medical services	4,201	6,861
Indigent care	<u>17,793</u>	<u>15,972</u>
	<u>\$ 21,994</u>	<u>\$ 30,056</u>

Assets released from restrictions were as follows:

	<u>Year ended June 30,</u>	
	<u>2008</u>	<u>2007</u>
Emergency medical services and equipment...	\$ 9,993	\$ 10,607
Hospital services and equipment	48,595	17,721
Indigent care	12,325	15,128
Bio-terrorism preparedness	<u>5,408</u>	<u>17,403</u>
	<u>\$ 76,321</u>	<u>\$ 60,859</u>

### **3. CASH AND ASSETS WHOSE USE IS LIMITED (continued)**

#### **Deposits**

Custodial credit risk for deposits is the risk that in the event of bank failure, the Hospital's deposits may not be returned or the Hospital will not be able to recover collateral securities in the possession of an outside party. The Hospital's policy follows applicable State statutes and requires deposits to be 100% secured by collateral (pledged securities) valued at market, less the amount of the Federal Deposit Insurance Corporation (FDIC) insurance. State statutes define the allowable pledged securities.

The Hospital's cash and investments at June 30, 2008 consisted of cash on hand, demand deposit, money market, and savings accounts. At year end, the carrying amount of the Hospital's deposits was \$1,751,269 with the bank balances of such accounts being \$1,785,089. Of the bank balances, \$200,000 was secured by federal depository insurance and \$1,585,089 was covered by collateral held by the Hospital's custodial banks in joint custody in the name of the Hospital and its banks. The fair value of those pledged securities held by the Hospital's custodial banks was \$2,233,492 at June 30, 2008.

#### **Investment policies**

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligation. The Hospital's investing activities are managed under the custody of the Hospital Chief Executive Officer. Investing is performed in accordance with investment policies adopted by the Board of Directors and in compliance with State statutes.

Applicable state statutes authorize the Hospital to invest in (1) temporary notes or no-fund warrants issued by the Hospital (2) time deposit, open accounts or certificates of deposit, with maturities of not more than two years, in commercial banks; (3) time certificates of deposit, with maturities of not more than two years, with state or federally chartered savings and loan associations or federally chartered savings banks, (4) repurchase agreements with commercial banks, state or federally chartered savings and loan associations or federally chartered savings banks; (5) United States treasury bills or notes with maturities as the governing body shall determine, but not exceeding two years; (6) the municipal investment pool maintained by the State Treasurer's office, and (7) trust departments of commercial banks.

### **4. CONCENTRATIONS OF CREDIT RISK**

The Hospital grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. The mix of gross accounts receivable from patients and third-party payors was as follows:

	June 30,	
	2008	2007
Medicare	\$ 972,436	\$ 809,191
Medicaid	55,835	84,761
Blue Cross	391,703	486,105
Commercial	270,980	237,090
Durable medical equipment	38,844	34,804
Self pay	513,443	511,388
	<u>\$ 2,243,241</u>	<u>\$ 2,163,339</u>

## 5. REVOLVING CREDIT AGREEMENT

At June 30, 2008, the Hospital had \$1,000,050 of an unused revolving credit line with a local bank to be drawn upon as needed, with interest at a variable rate of 1.5% under the New York prime rate. The note is collateralized by accounts receivable, equipment, and inventory. The agreement expires on December 15, 2008.

## 6. PENSION PLAN

The Hospital maintains a mandatory contributory pension plan for all eligible employees. Eligibility is established by all employees 21 years of age or older who have completed one year of service and have been paid for 1,000 hours of service for the year. Employer contributions are computed at the rate of 4.5% on the first 20% of the social security wage base (SSWB) of annual compensation plus 9.0% of annual compensation in excess of the first 20% of the SSWB. Employee contributions are computed at the rate of 2.5% on the first 20% of the social security wage base (SSWB) of annual compensation plus 5.0% of annual compensation in excess of the first 20% of the SSWB. Benefits are funded by an annuity contract with an insurance company. The plan is funded for past service on an installment basis over the estimated remaining duration of employment from January 1, 1976 to the employee's normal retirement date. The total cost of the plan was \$269,191 and \$261,144 for 2008 and 2007, respectively. Benefits vest after three years of service with 100% vesting after seven years of service.

## 7. CAPITAL ASSETS

Capital asset additions, disposals, and balances for the years ended June 30, 2008 and 2007 were as follows:

	Balance At June 30, 2007	Additions	Disposals	Transfers	Balance At June 30, 2008
Capital assets not being depreciated:					
Land	\$ 56,273	\$ —	\$ —	\$ —	\$ 56,273
Capital assets being depreciated:					
Land					
improvements	272,405	—	—	—	272,405
Buildings	3,207,374	48,656	—	—	3,256,030
Fixed equipment	1,512,796	8,556	—	—	1,521,352
Movable equipment	5,010,303	246,562	—	—	5,256,865
Total capital assets being depreciated	10,002,878	303,774	—	—	10,306,652

## 7. CAPITAL ASSETS (continued)

	Balance At June 30, 2007	Additions	Disposals	Transfers	Balance At June 30, 2008
Less accumulated depreciation for:					
Land					
improvements	187,033	15,535	—	—	202,568
Buildings	1,878,607	126,627	—	—	2,005,234
Fixed equipment	1,243,824	47,087	—	—	1,290,911
Movable equipment	<u>3,479,991</u>	<u>514,078</u>	<u>—</u>	<u>—</u>	<u>3,994,069</u>
Total accumulated depreciation	<u>6,789,455</u>	<u>703,327</u>	<u>—</u>	<u>—</u>	<u>7,492,782</u>
Total capital assets being depreciated, net	<u>3,213,423</u>	<u>(399,553)</u>	<u>—</u>	<u>—</u>	<u>2,813,870</u>
Total capital assets, net	<u>\$ 3,269,696</u>	<u>\$ (399,553)</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 2,870,143</u>
	Balance At June 30, 2006	Additions	Disposals	Transfers	Balance At June 30, 2007
Capital assets not being depreciated:					
Land	<u>\$ 56,273</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 56,273</u>
Capital assets being depreciated:					
Land					
improvements	272,405	—	—	—	272,405
Buildings	3,196,345	11,029	—	—	3,207,374
Fixed equipment	1,477,735	35,061	—	—	1,512,796
Movable equipment	<u>4,945,030</u>	<u>65,273</u>	<u>—</u>	<u>—</u>	<u>5,010,303</u>
Total capital assets being depreciated	<u>9,891,515</u>	<u>111,363</u>	<u>—</u>	<u>—</u>	<u>10,002,878</u>
Less accumulated depreciation for:					
Land					
improvements	171,482	15,551	—	—	187,033
Buildings	1,751,591	127,016	—	—	1,878,607
Fixed equipment	1,189,463	54,361	—	—	1,243,824
Movable equipment	<u>2,944,558</u>	<u>535,433</u>	<u>—</u>	<u>—</u>	<u>3,479,991</u>

## 7. CAPITAL ASSETS (continued)

	Balance At June 30, 2006	Additions	Disposals	Transfers	Balance At June 30, 2007
Total accumulated depreciation	<u>6,057,094</u>	<u>732,361</u>	<u>—</u>	<u>—</u>	<u>6,789,455</u>
Total capital assets being depreciated, net	<u>3,834,421</u>	<u>(620,998)</u>	<u>—</u>	<u>—</u>	<u>3,213,423</u>
Total capital assets, net	<u>\$ 3,890,694</u>	<u>\$ (620,998)</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 3,269,696</u>

## 8. LONG-TERM DEBT

The following is a summary of changes in long-term debt for the years ended June 30, 2008 and 2007:

	Balance At June 30, 2007	Additions	Reductions	Balance At June 30, 2008	Amounts Due Within One Year
Notes payable and capital lease obligations:					
Notes payable	\$ 952,318	\$ 200,000	\$ 175,504	\$ 976,814	\$ 205,792
Capital lease obligations	<u>428,646</u>	<u>—</u>	<u>20,110</u>	<u>408,536</u>	<u>21,446</u>
	<u>\$ 1,380,964</u>	<u>\$ 200,000</u>	<u>\$ 195,614</u>	<u>\$ 1,385,350</u>	<u>\$ 227,238</u>

	Balance At June 30, 2006	Additions	Reductions	Balance At June 30, 2007	Amounts Due Within One Year
Notes payable and capital lease obligations:					
Notes payable	\$ 1,116,527	\$ —	\$ 164,209	\$ 952,318	\$ 174,020
Capital lease obligations	<u>447,503</u>	<u>—</u>	<u>18,857</u>	<u>428,646</u>	<u>20,110</u>
	<u>\$ 1,564,030</u>	<u>\$ —</u>	<u>\$ 183,066</u>	<u>\$ 1,380,964</u>	<u>\$ 194,130</u>

The Hospital has notes payable to a local bank with interest rates that range from 6.50% to 6.75% and are collateralized by real estate, accounts receivable, equipment, and inventory.

## 8. LONG-TERM DEBT (continued)

During the year ended June 30, 2008 the entered into a note payable agreement for \$200,000 with a local rural electric cooperative under provisions of the U.S. Department of Agriculture's (USDA) Rural Economic Development Loan Program. The note has an interest rate of 5% and is due in ten annual installments of \$20,000 principal plus interest accrued on the declining balance. The note is collateralized by an irrevocable letter of credit with a local bank securing the repayment of the declining balance.

Scheduled payments on the notes payable are as follows:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
Year ending June 30:			
2009	\$ 208,792	\$ 49,676	\$ 258,468
2010	220,891	36,577	257,468
2011	141,641	24,087	165,728
2012	72,261	19,293	91,554
2013	75,005	15,548	90,553
2014	77,863	11,691	89,554
2015	80,871	7,683	88,554
2016	59,490	3,706	63,196
2017	20,000	2,000	22,000
2018	<u>20,000</u>	<u>1,000</u>	<u>21,000</u>
	<u>\$ 976,814</u>	<u>\$ 171,261</u>	<u>\$ 1,148,075</u>

The Hospital leases certain facilities and equipment under a capital lease that expires in 2021. Interest incurred under the lease was \$27,060 and \$28,313 for the years ended June 30, 2008 and 2007, respectively. The following is an analysis of the financial presentation of the capital lease:

	<u>June 30,</u>	
	<u>2008</u>	<u>2007</u>
Buildings	\$ 358,813	\$ 358,813
Fixed equipment	118,927	118,927
Movable equipment	<u>43,308</u>	<u>43,308</u>
	521,048	521,048
Less accumulated depreciation	<u>201,003</u>	<u>176,409</u>
	<u>\$ 320,045</u>	<u>\$ 344,639</u>

## 8. LONG-TERM DEBT (continued)

The following is a schedule of future minimum lease payments under the capital lease together with the present value of the net minimum lease payments as of June 30, 2008:

Year ending June 30:

2009	\$ 47,170
2010	47,170
2011	47,170
2012	47,170
2013	47,170
2014	47,170
2015	47,170
2016	47,170
2017	47,170
2018	47,170
2019	47,170
2020	47,170
2021	<u>33,693</u>

Net minimum lease payments	599,733
Less amount representing interest	<u>191,197</u>

Present value of net minimum lease payments	408,536
Less current portion	<u>21,446</u>

Long-term portion	<u>\$ 387,090</u>
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## **ADDITIONAL INFORMATION**

# SCOTT COUNTY HOSPITAL, INC.

## PATIENT SERVICE REVENUE

	Year ended June 30,				
	2008				2007
	Inpatient	Outpatient	Swing Bed	Total	Total
Routine service	\$ 712,700	\$ 262,411	\$ 494,325	\$ 1,469,436	\$ 1,888,185
Nursery	85,800	—	—	85,800	52,200
Operating room	178,200	630,323	—	808,523	654,375
Delivery room	66,182	—	—	66,182	35,893
Anesthesiology	69,968	178,743	1,140	249,851	244,992
Radiology	36,490	431,777	10,945	479,212	544,650
MRI	6,950	160,006	2,568	169,524	202,698
CT scan	99,680	876,223	9,690	985,593	1,129,542
Mammography	—	98,681	—	98,681	96,804
Nuclear medicine	374	142,265	379	143,018	184,437
Ultrasound	5,400	216,750	—	222,150	203,630
Laboratory	151,142	1,334,153	51,178	1,536,473	1,373,244
Blood administration	21,386	13,617	5,307	40,310	95,987
Respiratory therapy	230,760	75,505	165,258	471,523	283,009
Physical therapy	13,044	314,467	67,012	394,523	320,919
Occupational therapy	4,836	51,269	27,904	84,009	66,411
Speech therapy	1,402	8,049	2,842	12,293	3,918
Electrocardiology	39,225	368,329	4,981	412,535	434,318
Medical supplies	226,800	278,989	53,423	559,212	709,412
Pharmacy	390,431	680,952	323,201	1,394,584	1,378,472
Treatment room	58,356	650,831	2,734	711,921	88,106
Specialty clinics	882	145,424	1,050	147,356	155,568
Emergency room	17,722	344,854	—	362,576	301,332
Clinic	611	2,049,701	—	2,050,312	1,983,850
Cardiac rehabilitation	—	25,604	—	25,604	2,365
Durable medical equipment	—	352,088	—	352,088	342,312
Home health	—	127,776	—	127,776	151,403
Ambulance	13,488	125,798	3,023	142,309	132,711
	<u>\$ 2,431,829</u>	<u>\$ 9,944,585</u>	<u>\$ 1,226,960</u>	13,603,374	13,060,743
Contractual adjustments				(3,478,476)	(3,566,147)
Bad debts				<u>(293,507)</u>	<u>(229,507)</u>
Net patient service revenue				<u>\$ 9,831,391</u>	<u>\$ 9,265,089</u>

# SCOTT COUNTY HOSPITAL, INC.

## OPERATING EXPENSES BY FUNCTIONAL DIVISION

	Year ended June 30, 2008					% of total operating expenses
	Salaries	Employee Benefits	Supplies and other	Deprec- iation	Total	
Routine services:						
Acute and swing bed	\$ 1,030,064	\$ —	\$ 54,058	\$ 30,314	\$ 1,114,436	11.40%
Nursery	20,569	—	948	1,712	23,229	.24
Total routine services	<u>1,050,633</u>	<u>—</u>	<u>55,006</u>	<u>32,026</u>	<u>1,137,665</u>	<u>11.64</u>
Ancillary services:						
Operating room	96,059	—	61,543	21,763	179,365	1.83
Delivery room	26,148	—	1,449	7,872	35,469	.36
Anesthesia	198,185	—	6,285	22	204,492	2.09
Radiology	137,798	—	28,979	1,819	168,596	1.72
MRI	—	—	56,073	—	56,073	.57
CT scan	47,115	—	117,274	145,752	310,141	3.17
Mammography	32,848	—	18,375	—	51,223	.52
Nuclear medicine	1,686	—	108,786	—	110,472	1.13
Ultrasound	23,876	—	18,927	358	43,161	.44
Laboratory	196,518	—	251,859	8,063	456,440	4.66
Blood administration	2,833	—	23,479	—	26,312	.27
Respiratory therapy	111,986	—	7,925	6,355	126,266	1.29
Physical therapy	121,339	—	29,172	3,161	153,672	1.57
Occupational therapy	42,430	—	4,952	—	47,382	.48
Speech therapy	8,248	—	1,797	—	10,045	.10
Electrocardiology	41,131	—	1,992	6,938	50,061	.51
Medical supplies	22,551	—	127,163	2,256	151,970	1.55
Pharmacy	60,152	—	456,246	3,051	519,449	5.31
Treatment room	10,125	—	—	—	10,125	.10
Specialty clinics	51,694	—	17,816	882	70,392	.72
Emergency room	49,669	—	5,301	381	55,351	.57
Clinic	1,260,002	—	121,248	81,813	1,463,063	14.95
Cardiac rehabilitation	7,734	—	16,760	130	24,624	.25
Durable medical equipment	63,635	—	150,420	11,243	225,298	2.30
Home health	99,273	—	20,029	—	119,302	1.22
Ambulance	85,158	—	26,816	37,521	149,495	1.53
Total ancillary services	<u>2,798,193</u>	<u>—</u>	<u>1,680,666</u>	<u>339,380</u>	<u>4,818,239</u>	<u>49.21</u>
General services:						
Nursing administration	97,835	—	10,758	—	108,593	1.11
Operation of plant	75,871	—	269,705	1,612	347,188	3.55
Laundry	35,424	—	8,845	1,104	45,373	.46
Housekeeping	124,685	—	23,186	761	148,632	1.52
Nutritional services	135,469	—	103,735	2,941	242,145	2.47
Health information	213,035	—	48,532	6,872	268,439	2.74
Administration and general	650,590	—	502,263	202,709	1,355,562	13.85
Employee benefits	63,718	1,041,238	66,272	—	1,171,228	11.96
Depreciation-fixed equipment and buildings	—	—	—	145,910	145,910	1.49
Total general services	<u>1,396,627</u>	<u>1,041,238</u>	<u>1,033,296</u>	<u>361,909</u>	<u>3,833,070</u>	<u>39.15</u>
Total expenses	<u>\$ 5,245,453</u>	<u>\$ 1,041,238</u>	<u>\$ 2,768,968</u>	<u>\$ 733,315</u>	<u>\$ 9,788,974</u>	<u>100.00%</u>

	Year ended June 30, 2007					
	Salaries	Employee Benefits	Supplies and other	Depreciation	Total	% of total operating expenses
Routine services:						
Acute and swing bed	\$ 946,805	\$ —	\$ 24,926	\$ 30,401	\$ 1,002,132	10.40%
Nursery	15,559	—	1,174	1,712	18,445	.19
Total routine services	962,364	—	26,100	32,113	1,020,577	10.59
Ancillary services:						
Operating room	99,725	—	37,490	18,939	156,154	1.62
Delivery room	17,042	—	1,246	7,261	25,549	.27
Anesthesia	198,400	—	7,198	22	205,620	2.14
Radiology	132,590	—	61,266	3,873	197,729	2.06
MRI	—	—	67,731	—	67,731	.70
CT scan	50,564	—	60,742	145,752	257,058	2.67
Mammography	28,386	—	17,983	—	46,369	.48
Nuclear medicine	1,712	—	140,336	—	142,048	1.48
Ultrasound	23,129	—	16,852	25,358	65,339	.68
Laboratory	189,872	—	208,150	8,092	406,114	4.22
Blood administration	3,786	—	42,633	—	46,419	.48
Respiratory therapy	85,726	—	2,942	6,278	94,946	.99
Physical therapy	114,283	—	12,213	3,161	129,657	1.35
Occupational therapy	38,126	—	1,480	—	39,606	.41
Speech therapy	3,852	—	—	—	3,852	.04
Electrocardiology	45,950	—	7,936	6,938	60,824	.63
Medical supplies	18,709	—	130,425	2,588	151,722	1.58
Pharmacy	61,459	—	359,311	8,145	428,915	4.46
Treatment room	2,442	—	—	—	2,442	.03
Specialty clinics	57,898	—	17,758	1,316	76,972	.80
Emergency room	41,036	—	1,521	802	43,359	.45
Clinic	1,462,275	—	167,109	81,247	1,710,631	17.78
Cardiac rehabilitation	—	—	—	130	130	.00
Durable medical equipment	77,951	—	150,252	11,251	239,454	2.49
Home health	112,422	—	14,380	—	126,802	1.32
Ambulance	75,749	—	27,177	38,968	141,894	1.47
Total ancillary services	2,943,084	—	1,554,131	370,121	4,867,336	50.60
General services:						
Nursing administration	106,534	—	10,356	—	116,890	1.21
Operation of plant	79,780	—	238,048	1,612	319,440	3.32
Laundry	25,721	—	6,890	1,104	33,715	.35
Housekeeping	126,545	—	19,608	761	146,914	1.53
Nutritional services	130,481	—	101,853	2,941	235,275	2.45
Health information	209,650	—	45,001	6,889	261,540	2.72
Administration and general	595,663	—	508,800	193,234	1,297,697	13.49
Employee benefits	61,409	1,053,179	53,532	—	1,168,120	12.14
Depreciation-fixed equipment and buildings	—	—	—	153,574	153,574	1.60
Total general services	1,335,783	1,053,179	984,088	360,115	3,733,165	38.81
Total expenses	\$ 5,241,231	\$ 1,053,179	\$ 2,564,319	\$ 762,349	\$ 9,621,078	100.00%